United States Court of Appeals

for the Second Circuit

BRIEF FOR APPELLANT

To be argued by
SAMUEL M. SPRAFKIN

74-2615

United States Court of Appeals

SECOND CIRCUIT

MAURICE GOLDBERG, CLAIRE GOLDBERG, MAURICE GOLDBERG, as Custodian for MARION GOLDBERG, BETTE GOLDBERG and JOYCE E. GOLDBERG, under The New York Uniform Gifts to Minors Act, and MAURICE GOLDBERG, HENRY J. GOLDBERG and SAMUEL M. SPRAFKIN, as Trustees under the Trusts for the benefit of MARION GOLDBERG, BETTE GOLDBERG and JOYCE E. GOLDBERG,

Plaintiffs-Appellants,

—against—

ARROW ELECTRONICS, INC.,

Defendant-Appellee,

—and—

STATE OF NEW YORK,

Defendant.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF NEW YORK

BRIEF FOR PLAINTIFFS-APPELLANTS

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Preliminary Statement

This civil rights action challenges the constitutionality of certain provisions of the New York Business Corporation Law. Hon. Jacob Mishler, Chief Judge of the Eastern Dis-

trict Court of New York, granted defendant's motion to dismiss the complaint holding that State action, as required by the Fourteenth Amendment, is not present. Plaintiffs appeal from the judgment dismissing their complaint.

Issues

1. Is State action present within the meaning of the Fourteenth Amendment when the New York Business Corporation Law, section 623, modifies the common law and permits a corporate merger over the objections of non-assenting shareholders; and then permits the corporation to abandon the merger eight months later, terminating the judicial appraisal proceeding which the statute had compelled the dissenters to commence and the State court, in enforcing the statute, precludes the dissenters from claiming damages and losses sustained?

2. Upon the corporation's subsequent unilateral abandonment of the merger, were the non-assenting shareholders deprived of due process when the statute (i) deprived them of their property without compensation, and (ii) denied them a forum in which to be heard and have an adjudication of their claim for damages, losses and the expense of the proceeding which they were compelled to commence?

Statement of the Case

Nature of the Action

The complaint is by shareholders holding less than five percent of the shares in defendant corporation. They seek a judgment declaring a provision of Section 623 of the New York Business Corporation Law (BCL §623) unconstitutional insofar as it is applicable to an abandonment of a corporate merger.

After approval of the corporate merger by the shareholders other than plaintiffs, plaintiffs complied with the statute. They gave up their shareholder status. They became monetary claimants for the value of their shares. To preserve their rights they were compelled to and did commence the statutory judicial proceeding. Eight months later, defendant adanboned the merger. By virtue of the statute, such abandonment automatically terminated the proceeding and deprived plaintiffs of their rights. The statute reinstated plaintiffs to shareholder status eight months later. However, by virtue of the statute, plaintiffs were not restored to the position they were in eight months earlier. During that period plaintiffs' shares could not be traded on the stock exchange because of the statutory legend endorsed on the certificates. During that eight-month period the shares had declined in price and in value. By virtue of the statute, defendant's abandonment of the merger deprived plaintiffs not only of the right to be compensated for the value of their shares, but also of losses and damages sustained during the eight-month period they were monetary claimants. The statute deprived plaintiffs of a forum in which to be heard with respect to their claim for losses, damages, costs and expenses.

Plaintiffs claim that they were deprived of their property, rights and remedies, without due process, in violation of the Fourteenth Amendment. This was done by the corporate defendant solely by virtue of the statute. The State's legislative and judicial conduct constitutes State action, under the Fourteenth Amendment.

Course of Proceedings

The STATE OF NEW YORK was named as a defendant because the action questions the constitutionality of a State statute. The State appeared by its Attorney General and waived service of all papers and notices of all proceedings, with certain exceptions not applicable herein.

Defendant, ARROW ELECTRONICS, INC., answered, asserting three affirmative defenses. Reference in this brief to defendant is to the corporation and not the STATE OF NEW YORK.

Plaintiffs moved for summary judgment, pursuant to Rule 56 (44a). Defendant also moved for summary judgment pursuant to Rule 56, on the ground that plaintiffs' claim is barred by res judicata (19a). Defendant's supplementary motion (43a) for summary judgment was based on the ground that there is no issue of fact and that the State statute is constitutional as a matter of law. Defendant's supplementary motion was in the alternative, to dismiss the complaint for failure to state a claim upon which relief can be granted pursuant to Rule 12(b)(6).

Disposition of the District Court (178a)

The District Court denied plaintiffs' motion for summary judgment and granted defendant's motion to dismiss under Rule 12(b)(6). It found that there was no State ac-

tion, because the position of shareholders, objecting to a corporate merger, is virtually the same now under the statute as it would have been under the common law. The District Court also concluded that the statute does not violate the due process clause of the Fourteenth Amendment. The Court found nothing arbitrary or irrational in the statute and stated that it is rationally related to a sound and legitimate State interest.

Having granted defendant's motion to dismiss under Rule 12(b)(6), the Court did not consider defendant's motion for summary judgment.

Facts

Background and Proceedings at Special Term of the New York Supreme Court

Defendant is a New York corporation (121a). For some 25 years it was engaged in the electronics distribution business. It then embarked on a series of mergers and acquisitions. Some of these were entirely unrelated to its electronics distribution business. Plaintiffs were of the opinion that the acquisitions, which were unrelated to its original business, were not in the best interest of defendant and its shareholders (73a-74a, 96a-97a).

In its proxy statement for the annual meeting of its shareholders on May 25, 1972, defendant stated that it intended to pursue its acquisition opportunities. In order to do so, it proposed to change the State of its incorporation from New York to Delaware, because Delaware's "laws are generally more favorable to corporate expansion through mergers" (73a-74a, 76a, 96a).

In anticipation of its shareholders' authorization, defendant formed a "shell" or wholly owned subsidiary Delaware corporation of the same name, into which it would merge the defendant (86a-87a, 121a).

Attached to the notice to shareholders of the meeting was the merger agreement. It provided for "its abandonment by Arrow—even after stockholder approval" at any time prior to "its effective date." The effective date was defined as of the date of filing the merger agreement with the Secretary of State of Delaware (87a, 121a-127a).

Because the change in the State of incorporation from New York, where the corporate laws were more solicitous and protective of the rights of shareholders, would adversely affect plaintiffs as shareholders, they duly objected (5a, 68a).

Defendant had slightly more than 1,500,000 shares issued and outstanding. They were listed for trading on the American Stock Exchange (5a, 86a, 121a). On the date prior to the shareholders' meeting, the shares traded at a high of $10.375 and a low of $10.00 (131a). Plaintiffs held approximately 75,000 shares or slightly less than 5% of the outstanding shares (2a-4a, 86a).

The shareholders' meeting was held on May 25, 1972 (6a). Defendant then knew the number of objecting shares. It knew the trading prices of the previous day. It knew it required no less than $750,000. However, defendant had no money to pay for the shares of dissenting shareholders (89a). Furthermore, defendant's existing loan agreements did not permit it to pay for such shares (47a, 122a). Nevertheless, the merger was authorized by the shareholders other than plaintiffs (6a).

Plaintiffs, as dissenting shareholders, then followed the precise procedural steps required by BCL §623. They delivered their certificates, which were then endorsed with the statutory legend (6a-8a). Thus, they no longer had any rights as shareholders, except the right to be paid the fair value of their shares as of May 24, 1972, which is the day prior to the shareholders' authorization meeting. The shares could not be sold or traded. A transferee merely would stand in the shoes of his transferor-dissenting shareholder (97a-98a, 189a).

Despite the prohibition in its existing loan agreement (122a) and its recognition that consummation of the merger was financially impractical because it lacked the money to pay for any dissenter's shares (89a), defendant did not then abandon the merger. Instead, it embarked on a game of "heads I win, tails you lose." When the trading price of the shares increased, defendant moved forward. When the price declined, it did nothing. Defendant was not about to commit itself to acquire shares which were trading for less than what they would be required to pay by order of the court. An essential element of its game was to gain time for itself (47a-48a).

The statute, §623(g), required that defendant make a fair offer for plaintiffs' shares within 90 days from the shareholders' meeting of May 25, 1972. The 90-day period expired August 23, 1972 (118a). Defendant waited until the last day, when shares were traded at $10.625 (high) and $10.125 (low) (133a).

Defendant offered $9.00 per share, conditioned upon consummation of the merger into the Delaware corporation. No statement was made when the merger would occur

(7a). Defendant knew that the merger might never be carried into effect (85a). Defendant did not have $675,000 or $9.00 per share to purchase the shares (89a). Defendant's existing loan agreements did not permit any such payment (122a).

Defendant had 20 days, from September 18 through October 7, 1972, in which to commence its judicial appraisal proceeding but did not (7a). Its failure to do so, no doubt, was because the shares declined to a low of $8.50 and a high of $9.75 (133a-134a).

Because of defendant's failure to do so, plaintiffs were required to and did commence the statutory proceeding in the New York Supreme Court, pursuant to BCL §623. This was to determine their rights to be paid the fair value of their shares as of May 24, 1972, with interest, costs and expenses of the proceeding (59a-67a).

At Special Term of the New York Supreme Court (Murtagh, J.), defendant asserted that its offer of $9.00 was conditioned upon ultimate consummation of the merger, that it lacked the money, that its cash was needed for its day-to-day working capital requirements, and that it was negotiating with its principal institutional lender to increase its capital resources to obtain additional cash, so that it could go forward with its merger. Defendant asked that the proceeding be dismissed or held in abeyance, pending those negotiations (88a-90a).

On December 18, 1972, while the application was awaiting decision by the State court, defendant announced to Dow-Jones and financial analysts that it expected to complete arrangements by December 28 for a $8.4 million loan,

which would refinance all of defendant's debts and take care of its financing needs for the next three years (114a).

On January 9, 1973, twelve days after defendant had consummated its loan, the decision of Murtagh, J. appeared in the New York Law Journal. This was some seven months after the shareholders' authorization of the merger. He denied the application without prejudice to renewal, either upon consummation of the merger or the passage of an unreasonable period of time without consummation or abandonment of the merger. He found that defendant was negotiating "to obtain sufficient additional cash to make it feasible to go forward with the corporate action," that there had not been an unreasonable delay in defendant's failure to act, and that it would be premature to grant the motion (92a-93a). Plaintiffs appealed (29a, 53a).

On the day of publication of that decision, the trading price of the shares increased to a high of $10.50 and a low of $9.75 (135a). On that day, defendant initiated settlement discussions (109a-110a). The parties negotiated from January 16th through January 29, 1973. On January 31, 1973 the shares declined, trading at $8.625, low, and $8.875, high. On February 1 the shares further declined, trading at $8.375 (136a). On February 2 defendant notified plaintiffs that on January 31 its Board of Directors had abandoned the merger (105a, 101a).

Plaintiffs then moved at Special Term of the New York Supreme Court for additional relief, requesting damages, counsel fees, expenses, costs and disbursements (94a). Their application came on to be heard before Chimera, J. He denied all relief, except counsel fees, and referred the issue of the amount to the State court's special referee.

He found no basis in BCL §623 for any relief to plaintiffs, except subparagraph (h)(7) for counsel fees (139a-140a). Both parties appealed (29a, 53a).

The appeal from the determination of Murtagh, J. and the cross-appeals from the determination of Chimera, J. were heard simultaneously. No constitutional issue was raised.

The Appellate Division's Determination of the Appeal

On September 30, 1973, the Appellate Division of the State Supreme Court unanimously affirmed the order of Murtagh, J. and modified the order of Chimera, J. It denied all relief to plaintiffs. In its opinion, it held that the statutory scheme for regulation of corporate mergers and the comprehensive provisions for protection of dissenting shareholders did not make any provision for the relief granted or withheld by the Special Term. It concluded that plaintiffs should be denied all relief requested (145a-147a).

Plaintiffs Are Frustrated in Their Attempts to Raise the Constitutional Issue in the State Courts

On their appeal to the New York Court of Appeals as of right, plaintiffs sought to raise the constitutional issue (148a). However, their appeal was dismissed upon the ground that plaintiffs could not appeal as of right. The Court did not consider the constitutional question (150a, 151a).

Plaintiffs returned to the Appellate Division. They requested reconsideration because the statute, as interpreted by it, is unconstitutional. Plaintiffs, in the alternative, asked for leave to appeal to the Court of Appeals (152a-153a). The Appellate Division denied reconsideration and

denied permission to appeal (175a). It did not rule on the constitutional issue. Plaintiffs then moved in the New York Court of Appeals for permission to appeal (170a). It denied plaintiffs' application. It did not rule on the constitutional question (177a). No State court ruled on the constitutional issue.

ARGUMENT

I.

State action is present within the meaning of the Fourteenth Amendment. BCL §623 modifies the common law. It permits a corporate merger over the objections of non-assenting shareholders. It then permits the corporation to abandon the merger eight months later, terminating the judicial appraisal proceeding which the statute compelled the dissenters to commence. The State court, in enforcing the statute, precluded the dissenters from claiming damages and losses sustained.

The Common Law

At common law unanimous shareholder consent was required for a corporate merger, sale of assets or any fundamental change in the corporation. *In Re Clark's Will,* 257 N.Y. 487, 493 (1931). A shareholder with but one share could veto any such transaction. Because the courts adhered to the common law, corporations turned to the State to compel dissenting shareholders to submit to changes which the controlling majority desired, even though the effect of such changes is substantially to alter the nature of the investment of the dissenters.

VORENBERG: EXCLUSIVENESS OF DISSENTING SHAREHOLDER'S APPRAISAL RIGHT, 77 Harv. L. Rev. 1189, 1194.

As a result, in 1893 New York enacted its "appraisal" statute. It removed the requirement for unanimity for corporate change. Under such statute the non-assenting shareholder must submit to changes or be compensated.

DISSENTING SHAREHOLDERS RIGHT TO APPRAISAL, 28 N.Y.U. Law Rev. 1021.

In 50 BOSTON UNIVERSITY LAW REVIEW 57 at page 59 it is stated:

> "At common law a negative vote by a single shareholder would veto transactions, such as a merger, which resulted in fundamental changes in the structure of the corporation. The common law rule, requiring consent of all the shareholders, viewed a corporate charter as a contract between the corporation and all of its shareholders which could not be impaired without the consent of all parties to the contract. In order to grant the corporation the necessary flexibility—thereby the power to pursue changes which the majority desires—it became necessary to compel objecting shareholders to submit, although the nature of their contract would be altered against their will. The quid pro quo which the shareholders received for the power granted to the corporation is represented in the present appraisal statutes."

The Predecessor to the Present Abandonment Clause

Before 1950, the appraisal statute contained no provision for abandonment of a corporate merger or other

fundamental change after the vote of the shareholders. In amending the statute (Stock Corporation Law §21) in 1950, a clause was included permitting the unilateral abandonment by the corporation of a merger or other corporate action after adoption by the shareholders. See Chapter 647 of the Laws of 1950, ¶6 (197a).

The following year a corporation, utilizing such statutory provision, submitted to its shareholders a resolution containing a reservation to abandon after the shareholders vote. The case reached the New York Court of Appeals in 1954. The case is significant because what was foreseen by the State court's minority then is precisely what happened in the case at bar.

There Judge Fuld, in *Matter of McKinney,* 306 N.Y. 207 (1954), writing for a minority of three judges, viewed the right to abandon the merger as a device "to cheat minority shareholders" (at page 215). The four judge majority had held that the dissenting shareholders had lost their right to recover the value of their shares because they had failed to adhere strictly to the statutory timetable, this despite the fact that the directors had not proceeded wih consummation of the merger. Judge Fuld's language is descriptive of the statute. He wrote at page 219:

> "Indeed, by reason of other requirements of the statute's time table, such a proceeding is more than an anomaly; it may actually become a potent instrument for oppression. The stockholders' vote terminates the dissenter's rights as a stockholder and limits his claim solely to the ultimate award, and he may not thereafter resume his status as a stockholder without the consent of the corporation. Within twenty days after the vote,

the stockholder must send his certificate to the corporation for appropriate notation, so that the rights of innocent third persons may not intervene. This means, not only that his interest becomes, in effect, nonsalable, but that he is deprived of current income that he would otherwise have received in the form of dividends. * * *

"Such consequences as these, I venture, account for the form of the resolution here adopted. Those in control of the corporation were seeking a means to force the preferred stockholders to accept the 'voluntary' plan, while at the same time depriving them of the right to appraisal which the legislature intended them to have as an alternative. * * * If that sort of vote and action is permissible, then—as was said, though in an entirely different context, Garner v. Board of Public Works of City of Los Angeles, 341 U.S. 716, 728, 71 S.Ct. 909, 916, 95 L.Ed. 1317, per Frankfurter, J.—'All but the hardiest may well hesitate' to voice their dissent. In truth, under the circumstances present in this case, the right to appraisal, intended to protect dissenting shareholders, ceases to be a right and becomes a trap. 'All of these corporation statutes', we wrote in Small v. Sullivan, 245 N.Y. 343, 354, 157 N.E. 261, 264, 'have their legitimate purposes, but they cannot be used as a blind'."

Hornstein in CORPORATION LAW AND PRACTICE describes the abandonment clause as follows:

"The corporation may at will abandon its proposed action, whether or not the shareholder has diligently taken all steps necessary in the appraisal proceeding. By contrast, the shareholder usually cannot withdraw

his appraisal proceeding without consent of the corporation. * * * " (at page 182)

"The statutory procedure is reminiscent of a combination of medieval legal procedure and a modern-day children's game, 'Simple Simon Says'! The courts have 'played along' by construing the statute to permit the shareholders' meeting to vote a change 'subject to approval by the Board of Directors.' This technique compels the dissentient to commit himself before he can ascertain whether the action will be taken. If he does not file and the directors approve after the time period noted, it is too late for him to come within the statute. If he does file and they do not approve, his lot is not a happy one: his share certificate, having been 'stamped' to identify the shares as dissenting, is of questionable negotiability; for an indefinite period he is in a 'no-man's land' or worse; at a minimum, he is 'out' the fee of his own lawyer" (at page 184).

Although the majority in *Matter of McKinney* was adversely criticized and the minority opinion was found compelling in logic and justice (71 COLUMBIA LAW REV. 588, 605; 29 N.Y.U. Law Rev. 1589, 1594; 30 N.Y.U. Law Rev. 534, 546, and 1542, 1550), nevertheless, when the Stock Corporation Law was replaced in 1963 by the Business Corporation Law, the abandonment provision in substance was retained.

The Present Statute

The statute which confers on a non-assenting shareholder the right to be compensated is BCL §910. It is entitled: "Right of Shareholder to Receive Payment for Shares upon Merger". This section confers the right to

receive payment of the fair value of his shares upon a shareholder who does not assent to a plan of merger of his corporation into another corporation, which is to be the survivor. This right is subject to compliance by the shareholder with BCL §623.

Indeed, the sole and exclusive remedy available to a non-assenting shareholder is BCL §623. *Blumenthal* v. *Roosevelt Hotel,* 202 Misc. 988, 115 N.Y.S.2d 52; *Beloff* v. *Consolidated Edison Co.,* 300 N.Y. 11; *Anderson* v. *International Mineral & Chem. Corp.,* 295 N.Y. 343.

When plaintiffs dissented, their share certificates were endorsed with the statutory legend. They ceased "to have any of the rights of a shareholder". Their shares could not be traded in the marketplace. They no longer had control of their investment. In lieu thereof, the statute gave plaintiffs a monetary claim or right to be paid the fair value of their shares as of the day prior to the shareholders' authorization meeting. BCL §623(e).

Having acquired such right to be paid the fair value of their shares, plaintiffs were compelled to and did comply with all procedural requirements to preserve it.

When defendant failed to commence the judicial proceeding in the State Supreme Court pursuant to BCL §623 (h)(1) to determine the rights of dissenting shareholders and to fix the value of their shares, plaintiffs were compelled to do so under BCL §623(h)(2). Had plaintiffs neglected to commence the proceeding within the specified 30-day period, they would have lost their rights. And defendant would have proceeded with consummation of the merger without paying plaintiffs. *In Re McKinney,* 306 N.Y. 207; *Marcus* v. *R. H. Macy & Co.,* 297 N.Y. 38.

What the defendant did was wait for the dissentients to trip with respect to compliance with at least one of the many statutory requirements and thus lose their rights under the statute. Defendant embarked on a game of delay and of the corporate game of "heads I win, tails you lose." It accepted the share certificates of plaintiffs for endorsement, thus depriving them of their status as shareholders and relegating them to the position of monetary claimants for the value of their shares. Defendant waited the full 90-day period to make its knowingly inadequate and unacceptable offer of $9.00 per share and then only conditioned on consummation of the corporate merger without stating when it would occur. It failed to commence the appraisal proceeding, gaining for itself additional time. When plaintiffs commenced the proceeding, which they were required to do, in default of which they would have lost their rights, defendant requested additional time from the State court to negotiate a loan to consummate the corporate merger. The court (Murtagh, J.) did precisely what defendant requested.

All of the foregoing was not "routine corporate management only", but "chicanery" (at page 215 of 306 N.Y.).

In the case at bar, defendant abandoned the merger after the passage of more than eight months and after the value and price of the shares had declined. It did this because BCL §623 specifically provides that it may do so. Defendant acted with knowledge of its provisions. As was stated in *Adickes* v. *S. H. Kress & Co.*, 398 U.S. 144 (1970), an essential element for "taking actions under color of law is that the person act with knowledge of and pursuant to a state law".

Plaintiffs then brought on their application for alternative additional relief. It was in the then pending proceeding. It was not in a second action or proceeding, as the District Court mistakenly stated. It matters not in the action at bar that the Special Term of the New York Supreme Court partially granted and partially denied the relief claimed by plaintiffs. Nor does it matter that the Appellate Division modified such ruling although the District Court mistakenly stated that the rulings were affirmed. What does matter is the holding and interpretation of the statute made by the Appellate Division. The Appellate Division decided that, upon the abandonment of the corporate merger, plaintiffs were not entitled to be compensated for loss, damages or expenses, because the statute made no such provision. It denied all relief and a forum in which to present such claims.

The State legislation of which plaintiffs complain is the provision in BCL §623(e) and its counterpart, BCL §903 (b), which enables a corporation unilaterally to abandon its corporate merger.

Had there been no such statute, defendant would not have acted and plaintiffs would not have been deprived of their property nor suffered any loss, damage or the expense of a judicial proceeding.

The Fourteenth Amendment, Section 1, provides in part:

> "* * * No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of * * * property, without due process of law; * * *."

42 U.S.C. §1983 provides:

> "Every person who, under color of any statute * * * of any State * * * subjects, or causes to be subjected, any citizen of the United States or other person within the jurisdiction thereof to the deprivation of any rights, privileges, or immunities secured by the Constitution and laws, shall be liable to the party injured in an action at law, * * * for redress."

The jurisdictional counterpart of §1983 is 28 U.S.C. §1343(3). It provides:

> "The district courts shall have original jurisdiction of any civil action authorized by law to be commenced by any person: * * *
>
> "(3) To redress the deprivation, under color of any State law, statute, ordinance, regulation, custom or usage, of any right, privilege or immunity secured by the Constitution of the United States * * *."

In *Lynch* v. *Household Finance Corp.*, 405 U.S. 538 (1972), the Supreme Court held that the "right to enjoy property without unlawful deprivation" is a personal right, and within §1343(3).

The District Court used the language of this Court in *Shirley* v. *State National Bank of Connecticut*, 493 F.2d 739, 741 (1974) when it stated that "since the Civil Rights Cases, 109 U.S. 3 (1883), it has been recognized that the Fourteenth Amendment applies only to actions of the 'States' and not to actions which are 'private.'" The District Court's footnote continues and paraphrases the balance of this Court's language: "The 'under color of State

law' provision in section 1983 is equivalent to the State action requirement of the Fourteenth Amendment."

In the *Civil Rights Cases,* the Supreme Court stated that the Fourteenth Amendment

> "* * * nullifies and makes void all State legislation, and State action of every kind, which impairs the privileges and immunities of citizens of the United States, or which injures them in life, liberty or property without due process of law, or which denies to any of them the equal protection of the laws" (at p. 11 of 109 U.S.).

The District Court relied upon *Shirley* v. *State National Bank of Connecticut,* 493 F.2d 739 (2d Cir. 1974) in finding no State action. The District Court erred. *Shirley* supports plaintiffs' contention that State action is present. *Shirley* was an action by a conditional vendee against the assignee of her conditional vendor of the automobile which had been peacefully repossessed by the assignee. The language of this Court with respect to "state action" is significant:

> "How then has the State of Connecticut become sufficiently implicated so that the seizure can be interpreted as state action? Plaintiff argues that Conn. Gen. Stat. Rev. § 42-98(a) authorizes the retaking. But if the peaceful repossession of the chattel authorized by the contract is valid in any event, how does the statute constitute a state involvement? The first inquiry must be, whether, absent a state statute, a Connecticut creditor would have the self-help remedy complained of. There is no dispute but that under the common law of Connecticut, the right of peaceful repossession without a hearing was recognized. (Citing cases) The

statute in Connecticut, therefore, does not create any right otherwise unavailable" (at 741-2).

"As we have indicated, since peaceful repossession existed at common law in Connecticut, the mere codification of that right does not, in our view, constitute state action. No delegation of traditional state power has been granted to any private person" (at 743).

BCL §623 created rights, otherwise unavailable to the corporation under the common law.

Contrary to the common law, the statute permits the defendant corporation to merge and thus change the State of its incorporation without unanimous shareholder consent. The statute converts the non-assenting shareholder to the status of a monetary claimant for the value of his shares as of the day prior to shareholder approval. If the corporation fails to commence the judicial proceeding, the statute compels the dissenter to do so, in default of which he loses his rights under the statute. The statute permits the corporation to abandon the merger for any reason—even when the price and value of the shares have declined below what it would have been required to pay and at a time more than eight months after the shareholders' meeting. Such abandonment results in the termination of the judicial proceeding which the dissenters were compelled to commence. It reinstates them to the status of shareholders, but does not restore them to the position in which they were eight months earlier. During this period their shares have declined in value and price, they are monetary claimants, they have no control of their investment and their shares cannot be traded in the market place. The statute, as construed and enforced by the State court, deprives plaintiffs

of their property without compensation and denies them a forum in which to present their claim for loss, damages and expenses incurred and an opportunity to be heard. This is State action.

In *Shelley* v. *Kraemer,* 334 U.S. 1 (1948) the Supreme Court stated:

> "That the action of state courts and judicial officers in their official capacities is to be regarded as action of the State within the meaning of the Fourteenth Amendment, is a proposition which has long been established by decisions of this Court." (at page 14)
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> • • • • •
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> "Similar expressions, giving specific recognition to the fact that judicial action is to be regarded as action of the State for the purposes of the Fourteenth Amendment, are to be found in numerous cases which have been more recently decided. In Twining v. New Jersey, 211 U.S. 78, 90-91 (1908), the Court said: 'The judicial act of the highest court of the State, in authoritatively construing and enforcing its laws, is the act of the State.' In Brinkerhoff-Faris Trust & Savings Co. v. Hill, 281 U.S. 673, 680 (1930), the Court, through Mr. Justice Brandeis, stated: 'The federal guaranty of due process extends to state action through its judicial as well as through its legislative, executive or administrative branch of government' " (at page 15).
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> • • • • •
>
> "The short of the matter is that from the time of the adoption of the Fourteenth Amendment until the present, it has been the consistent ruling of this Court that the action of the States to which the Amendment has

> reference includes action of state courts and state judicial officials" (at page 18).

Reitman v. *Mulkey,* 387 U.S. 369 (1967), cited in *Shirley,* is illustrative of "state action" found lacking in *Shirley.*

> "That case involved an amendment to the California State Constitution, which barred the State from placing any limitation on the right of a person to dispose of his real property. The amendment, in effect, created a State Constitutional right to discriminate, repealing prior acts of the state legislature which had regulated racial discrimination in housing. The Supreme Court held that this effectively constituted state action which encouraged racial discrimination. The distinction is clear. The State of California by express Constitutional Amendment permitted what was formerly prohibited" (at 744 of 493 F.2d).

BCL §623 allowed the defendant to do precisely what the common law prohibited.

Blye v. *Globe-Wernicke Realty Co.,* 33 N.Y.2d 15, 347 N.Y.S.2d 170 (1973), was a declaratory judgment action involving the constitutionality of New York's Innkeeper Lien Law, allowing summary seizure by a hotel of a guest's personal property for nonpayment of hotel charges. There the court held that the action of the hotelkeeper, possessed of certain powers by virute of Section 181 of the Lien Law, "clothed" the hotelkeeper's action "with the authority of state law" and such "actions may be said to be those of the State for purposes of the due process clauses." In support thereof, the New York Court of Appeals relied on *United States* v. *Classic,* 313 U.S. 299 (1911).

In *Monroe* v. *Pape,* 365 U.S. 167 (1961), the Supreme Court quoted from *United States* v. *Classic*:

> "Misuse of power, possessed by virtue of state law and made possible only because the wrongdoer is clothed with the authority of state law, is action taken 'under color of' state law" (at page 184 of 365 U.S.).

The District Court viewed the position of plaintiffs under the statute as "virtually the same as it would have been under the common law," when they were "returned to their status as shareholders." The District Court appears to have disregarded completely the eight-month period during which plaintiffs had no control of their investment and their shares could not be traded in the market place. The District Court also appears to have disregarded completely that during this period of time the shares declined in price and value and that reinstatement to shareholder status did not restore plaintiffs to the position they were in eight months earlier. None of this could have occurred under the common law. It was done solely because the State by its statute, as construed and enforced by the State court, permitted the defendant to do so. There was State involvement. State action is present within the meaning of the Fourteenth Amendment.

II.

Under defendant's subsequent unilateral abandonment of the corporate merger, BCL §623(e) deprived plaintiffs of their property without compensation and denied them a forum in which to be heard and have an adjudication of their claim for damages and losses sustained, all without due process in violation of the Fourteenth Amendment.

The District Court stated that it is "quite clear that this section does not violate the due process clause of the Fourteenth Amendment." It held that the failure of the statute to provide plaintiffs with a vested right of compensation for their shares does not even approach the degree of arbitrary or irrational activity which must be present in order to upset the statute. The District Court is in error.

The statute did accord the plaintiffs, as dissenting shareholders, the right to receive the value of their shares. They could have been divested of that right upon abandonment of the merger and reinstatement to shareholder status in a constitutionally correct manner. All that need be done was to compensate them for their loss after a hearing.

The failure of the statute to make any such provision permitted the defendant to engage in an activity which is arbitrary and irrational.

When the merger was authorized on May 25, 1972, defendant knew the number of non-assenting shares [§623 (a)] and the trading price of the shares on the prior day. This provision of the statute was inserted so that the corporation could determine the cash needed for such purpose.

1934 BULLETIN OF COMMITTEE ON STATE LEGISLATION, ASSN. OF THE BAR OF THE CITY OF N. Y., page 639.

Defendant knew that it had no cash resources to pay for dissenters' shares and that its existing loan agreements did not permit the purchase of its shares. Nevertheless, defendant embarked on a statutory permissible scheme of playing a corporate game of "heads I win, tails you lose". If the value or price should rise above that of May 24, 1972, it was to the advantage of defendant to proceed. If the value or price should decline, it was to defendant's advantage to abandon the merger. This it did. This is the "arbitrary activity" which the statute permitted.

Under New York law, BCL §623 is the sole and exclusive remedy available to a shareholder who does not assent to the plan of merger. *Blumenthal* v. *Roosevelt Hotel,* 202 Misc. 988, 115 N.Y.S.2d 52; *Beloff* v. *Consolidated Edison Co.,* 300 N.Y. 11; and *Anderson* v. *International Mineral & Chemical Corp.,* 295 N.Y. 343.

When plaintiffs perfected their right to dissent, they had traded their shareholder status for that of a monetary claimant. Plaintiffs had a "significant property interest". Their claims, as of May 24, 1972, which was the statutory valuation date, even at American Stock Exchange trading prices, were in excess of $750,000.

By virtue of the statute, plaintiffs were compelled to commence the judicial proceeding. By virtue of the statute, defendant's unilateral act of abandoning the merger terminated that proceeding and deprived plaintiffs of the right to receive payment of the value of their shares, interest, attorney's fees and costs. Reinstatement to share-

holder status, after having their shares or investment "frozen" for a period of more than eight months, is not restoring plaintiffs to the position they were in eight months earlier. By virtue of the statute, plaintiffs were deprived of their property during this eight-month period. During this eight-month period they were unable to trade their shares in the market place. During this eight-month period their shares had declined in value and in price.

When the defendant unilaterally abandoned the merger, the statute automatically and arbitrarily foreclosed plaintiffs from prosecuting their claims for the value of their shares or for the damages they had sustained. It deprived them of a forum to be heard and have their claims presented. They were deprived of due process.

Fuentes v. *Shevin*, 407 U.S. 67 (1972);
Sniadach v. *Family Finance Corp.*, 395 U.S. 337 (1969);
Blye v. *Globe-Wernicke Realty Co.*, 33 N.Y.2d 15 (1973).

In *Fuentes (supra)*, the Supreme Court stated:

> "The constitutional right to be heard is a basic aspect of the duty of government to follow a fair process of decision making when it acts to deprive a person of his possessions. The purpose of this requirement is not only to ensure abstract fair play to the individual. Its purpose, more particularly, is to protect his use and possession of property from arbitrary encroachment—to minimize substantively unfair or mistaken deprivations of property, a danger that is especially great when the State seizes goods simply upon the application of and for the benefit of a private party" (407 U.S. 67 at pages 80-81).

The District Court concluded by stating "section 623 is rationally related to a sound and legitimate state interest." We agree that this is so with respect to compelling non-assenting shareholders to submit to corporate changes or take the statutory alternative and be compensated. However, it is not so when the State permits a corporation to play a "heads I win, tails you lose" game. There is nothing sound or legitimate in permitting a deprivation of property for eight months without provision for compensation or a hearing to determine whether there was any damage or loss which resulted from the unilateral act of abandonment.

> *Sugar* v. *Curtis Circulation Co.*, 383 F. Supp. 643 (S.D.N.Y., 3 judge court, 1974);
>
> *Clement et al.* v. *Four North State Street Corp.*, 360 F. Supp. 933 (D.C., N.H., 3 judge court, 1973).

The United States District Court for Southern Maine, in *Arrowhead Estates, Inc.* v. *Cumming*, 360 F. Supp. 1085 (1973), had before it a State statute which permitted pre-judgment attachment. Although the statute did not deprive the owner of the use of his property, the court found that the owner's right to alienate his property was entitled to constitutional protection. Constitutional protection was not afforded, because the State statute failed to comply with the hearing requirements of *Fuentes* v. *Shevin, supra.*

BCL §623 is unconstitutional when there is an abandonment of the corporate merger after the judicial appraisal proceeding has been commenced: in that it deprived plaintiffs, as dissenting shareholders, of their right to receive

from the corporate defendant payment of the value of their shares; in that it deprived plaintiffs of their property for more than eight months; in that it deprived plaintiffs of the right to trade their shares on the American Stock Exchange for more than eight months; in that it deprived plaintiffs of the right to be compensated for the damages sustained by reason of the decline in the value of their shares during the period of more than eight months; in that it deprived plaintiffs of the right to be compensated for costs and expenses, including attorney's fees, of the judicial proceeding which they were compelled to commence; all without due process.

CONCLUSION

State action is present within the meaning of the Fourteenth Amendment (a) when the State legislates and modifies the common law to permit (i) a corporate merger over the objections of non-assenting shareholders and (ii) an abandonment of the merger eight months later, terminating the judicial appraisal proceeding which the statute had compelled the dissenters to commence, and (b) when the State court, in enforcing the statute, forecloses the dissenters from claiming damages and losses which they sustained.

Upon defendant's unilateral abandonment of the merger after a lapse of eight months, BCL §623(e) deprived plaintiffs of their property without compensation and denied them a forum in which to be heard and have an adjudication of their claim for damages and losses sustained, all of which is without due process in violation of the Fourteenth Amendment.

The complaint states a cause of action under 42 U.S.C. §1983 and its jurisdictional counterpart, 28 U.S.C. §1343(3).

The judgment should be reversed and the complaint reinstated.

January 28, 1975

Respectfully submitted,

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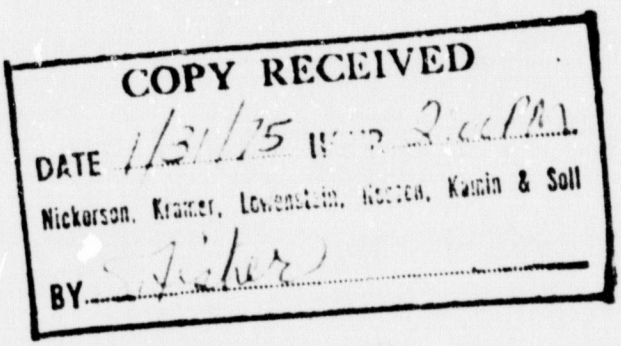
Service of two Copies of the within brief for Plaintiffs - Appellants is admitted

January 31st 1975

Attorneys for Appellee



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